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SUBJECT: Special autonomy in Aceh: governance challenges mounting

**¶1. (SBU) Summary:** The April legislative elections marked a major transition point for Aceh. A bigger challenge for Aceh: governance. Provincial, district and national government have struggled to implement their respective governance roles under special autonomy. The two biggest economic governance issues are provincial and district governments' ability to execute their budgets and the quality of spending. Many local governments cannot spend their budget outlays. And funds that are spent largely go to overhead costs. High turnover in provincial and local parliaments - estimated to be 60-80% - pose potential governance challenges based on the lack of experience of the new legislators. Support for special autonomy and Aceh's enhanced decentralization remains high. Yet, frustrations related to implementing special authority effectively are mounting. End Summary.

Implementation of special autonomy still lacking

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**¶2. (SBU) Special autonomy** - an expanded form of decentralization with even greater local authorities and resources - has enjoyed widespread support in Aceh since initial decentralization policies were established in 2001. In addition to normal decentralization funds, Jakarta has allocated special funds as part of the peace agreements to support Aceh's post-conflict transition from 32 years of conflict. Parliament passed an Aceh special autonomy law in 2001, which was revised in 2006. The 2005 Aceh governance law then gave further special autonomy rights, including the establishment of increased oil & gas revenue-sharing funds as well as tsunami and reintegration funds. The direct election of the Aceh Governor in 2006 was a critical step in the implementation of these special autonomy laws. District government (kabupaten/regency and kota/city) elections increased further confidence in special autonomy. The April 2009 legislative elections - with the participation of six local Acehnese political parties in addition to the 38 national parties - marked another milestone in the post-conflict transition.

**¶3. (SBU) Decentralization** in Aceh is implemented starting from the provincial down to the village level, eliciting support from all levels due to the greater local-level decision-making and resource allocation. However, budget implementation is slow and accountability is lacking. In addition, there are many legal and procedural uncertainties regarding decentralization in general and Aceh special autonomy specifically. Jakarta has not issued government regulations or presidential decrees to fully implement seven critical special autonomy policies (e.g., administration of oil & gas resources), according to senior Aceh provincial officials. These procedural delays and uncertainties have led to delays in budget allocation and project implementation.

Budget spending reflects wider governance problems

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**¶4. (SBU) Aceh provincial and district governments** have not been able

to fully spend their budgets, often placing large portions of the budget in reserve bank accounts. Aceh provincial and district governments spent on average 60% of their budget in 2007 and 45% of their budget in 2008, according to the World Bank. For those governments that are able to spend budget funds, the quality of spending is often poor. An estimated 60-70% of budget funds - sometimes more - are devoted to overhead expenses, particularly government salaries. In Bireuen District, 65% of the local budget is dedicated to salaries. This poor quality of spending reflects broader national trends.

**15.** (SBU) Aceh is a well-funded province. The provincial budget has rapidly increased over the past four years, totaling \$900 million (Rp 9 trillion; Rp 10,000 = 1 USD) in 2009 (2008 - \$830 million; 2007 - \$430 million; 2006 - \$200 million). Although reconstruction funds have ended, Aceh still receives special autonomy funds, special oil and gas revenues, regular budgetary outlays, and local tax revenue. Combined 2009 provincial and district government budgets could total up to \$1.9 billion, according to analysts and government officials. Lack of resources is not the problem; spending - particularly quality of spending - is the critical issue.

The provincial government spent 60% of its \$830 million budget in 2008 and 70% of its \$430 million budget in 2007. However, in absolute terms, Aceh still spent more in 2008 compared to 2007 due to annual budget increases.

**16.** (SBU) In addition to regular revenue flows from Jakarta and local income tax, Aceh receives special autonomy and oil & gas revenue-sharing funds. The special autonomy funds are 2% of the national government's general allocation fund (DAU) through 2021. In 2008, special autonomy funds totaled \$370 million and are scheduled to drop to \$250 million in 2009, according to the World

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Bank. The oil & gas funds are a special arrangement based on national legislation providing that 70% of Acehnese oil and gas profits be returned to the province (vice 40% for gas and 15% for oil for all other Indonesian provinces). The government requires 30% of these oil & gas funds to be spent on education. In 2008, Aceh received \$130 million in oil & gas funds, but oil & gas funds declined in 2009 to \$50 million due to the fall in the market price of oil.

**17.** (SBU) Administration of these special funds is a work in progress as there have been a number of national legislative and local administrative changes in recent years. The provincial government did not spend any of its oil & gas funds in 2008 due largely to limited administrative capacity; the oil & gas funds team was a three-person operation. The Aceh provincial government distributes 60% of the special autonomy and oil & gas funds directly to the district level and uses the remaining 40% for provincial government-led projects. The special autonomy funds on average account for about 10% of district government budgets. Project proposal and approval processes have delayed the disbursement of funds, tracking with overall budget expenditure difficulties.

**18.** (SBU) Aceh's special autonomy status - with its enhanced budget authorities and resources - increases the role of the provincial government compared to other Indonesian provinces. However, district governments still receive significant resources and have considerable budget authorities through standard district-level decentralization budget allocations. Coordinating with district governments, the Aceh provincial government has organized a new program - the "village budget allocation" - that provides \$15,000 (Rp 150 million) to each of the 6,300 plus villages of Aceh. In some districts, the village budget allocation is 8-10% of overall district discretionary spending. At the provincial level, every member of the provincial parliament receives \$500,000 in "aspiration funds" for local level projects. Corruption, poor quality of spending, and other misuse of funds are possible problems for these funds. However, these programs help to address the inability of provincial and district governments to spend their budgets.

Challenges to implementing decentralization in Aceh

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**¶9. (SBU)** Aceh's governance challenges reflect nationwide difficulties with decentralization implementation, but are compounded by post-conflict transition dynamics. Limited governance capacity in Aceh restricts economic growth and broader development. Human resource capacity is a top problem, according to government and civil society contacts. Poor infrastructure, limited local government capacity, and the proliferation of new districts have compounded governance challenges. The weak capacity of the Aceh provincial government is a bigger problem compared to other provinces due to the larger provincial level role under special autonomy. The Aceh provincial government has significant authorities related to the flow of budget funds, particularly special autonomy and oil & gas funds that make up the majority of funds available for development spending by districts.

**¶10. (SBU) HUMAN RESOURCES:** Poor human resources limit the effectiveness of provincial and district governments. Despite the sub-par workforce, some districts spend up to two-thirds of their budget on salaries. Compounding this problem, the April 2009 legislative elections will create 60-80% turnover in the provincial and local legislatures, described by some Acehnese as "tsunami politics." Most of these new MPs - largely from Aceh Party (PA) and some from Yudhoyono's Democrat Party (PD) - lack any governing experience. PA Secretary General Yahya and other PA leaders have reiterated their requests for legislative capacity-building at the provincial and district level in meetings with Mission Indonesia personnel.

**¶11. (SBU) INFRASTRUCTURE:** Analysts and government officials often cite infrastructure as an area that must continue to be a top government priority to improve economic development prospects. However, infrastructure spending is increasing at the provincial and district level and some benefits are becoming apparent. The average share of infrastructure spending of district government expenditures was over 16% in 2007, compared to 11% in 2004, according to the World Bank. Infrastructure, particularly roads and access to public services, varies across the province. There is a noticeable qualitative difference between infrastructure in coastal areas compared to more remote areas, such as Central Aceh, although some of the difference can be attributed to the lack of political support for the provincial government in these areas.

**¶12. (SBU) LOCAL GOVERNMENT CAPACITY:** District-level government capacity is even more limited than the provincial level. As is the

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case throughout Indonesia, there is a range in quality of governance throughout the district level in Aceh. Districts with weaker capacity often are delayed in their budgeting process or cannot complete the needed project proposals to utilize special autonomy funds administered by the provincial government. Beyond the budget approval process, budget implementation and oversight are weak, which leads to limited accountability.

**¶13. (SBU) PROLIFERATION OF NEW DISTRICTS:** The number of districts within Aceh has sharply increased since 2001: from 14 to 23. With every new district, there are more overhead expenses, particularly government buildings and salaries. Public service has worsened due to the proliferation of districts, according to most analysts. Most Acehnese government officials - including the Governor, PA leaders, and the district head who leads the Aceh local government forum - oppose further new district proposals. Yet, there are some new district proposals that originate from local leaders and are supported by the national parliament, allegedly due to bribes. Governor Irwandi and PA leaders are strongly opposed to any breakup of Aceh province into smaller subunits. PA leaders said that the establishment of breakaway provinces would violate the 2005 Helsinki MoU. However, there is the possibility of permitting some new districts, according to Aceh analysts and government officials.

**¶14. (SBU)** Performance varies widely among Aceh's 23 cities and districts. Quality of leadership at the district level is the single most important factor in determining a district's success, according to most analysts. The city of Banda Aceh has made marked improvements in public service delivery, transparency, and accountability. Banda Aceh was ranked as one of the least corrupt

local governments in Indonesia in a recent Transparency International survey. Some of the newly formed districts, such as Bireun, North Aceh and Lhokseumawe, have also managed the development process well. However, others struggle to develop, such as Subulussalam, Pidie Jaya, and Bener Meriah. Corrupt leadership in Bener Meriah has stunted growth despite potential wealth from coffee. Poor roads and infrastructure make it expensive for farmers to get their product to market. The provincial government also suffers from weak leadership and capacity. The Ministry of Home Affairs plans to evaluate the development status of the new districts and merge poorly performing districts back to their original district. However, this plan would face serious political obstacles at the local and national level.

Balancing national, provincial, district relationships

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¶15. (SBU) There is a complex set of relationships for budget allocation between the central government and Aceh provincial and district governments. The central government distributes funds to the Aceh provincial government (some of which are then sent to the district level) and other funds directly to the district level. Special autonomy and oil & gas funds are sent to the Aceh provincial government, who implements projects directly and also apportions funds to district governments. Normal decentralization funds (e.g., DAU - General Allocation Funds, DAK - Special Allocation Funds) go to both the provincial and district level. The provincial government divides its funds among the 23 districts after districts propose projects and budget plans have been approved by district parliaments. Local governments also seek community input through public consultation processes (Musrembang). General Allocation Funds (DAU) can be placed in bank trusts if unused and saved for the following year. Special Allocation Funds (DAK) must be used during the year in which they are disbursed or they are returned to Jakarta.

¶16. (SBU) Overlapping authorities have led to difficulties in Aceh's special autonomy implementation (e.g., which level of government has permit authorities for certain approvals). For example, overlapping authorities have delayed implementation of the Sabang Free Trade Zone. District governments also often issue regulations that contradict provincial or national laws. In addition, some national laws related to special autonomy are still awaiting implementing regulations, which creates regulatory and legal uncertainty.

Aceh: moving to next stage of governance transition

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¶17. (SBU) The biggest "X factor" for Aceh's future is the governance of PA in the provincial and district legislatures. Government and civil society contacts said that legislative governing capacity will be limited with 60-80% new MPs coming into provincial and district parliaments. PA has a near majority in the provincial parliament (33 of 69 seats) and majorities in many district parliaments. To what extent will PA engage in rent-seeking and other corrupt practices? Bireuen's district head - who is also head of the Aceh Local

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Government Forum - acknowledged the possibility for corrupt behavior and said that he would only tolerate a "certain amount" of this rent-seeking. PA Secretary General Yahya directly requested legislative capacity building programs to bolster PA's limited governing capacity. PA has set out an agenda that includes anti-corruption reform and broader governance to improve government performance.

NORTH